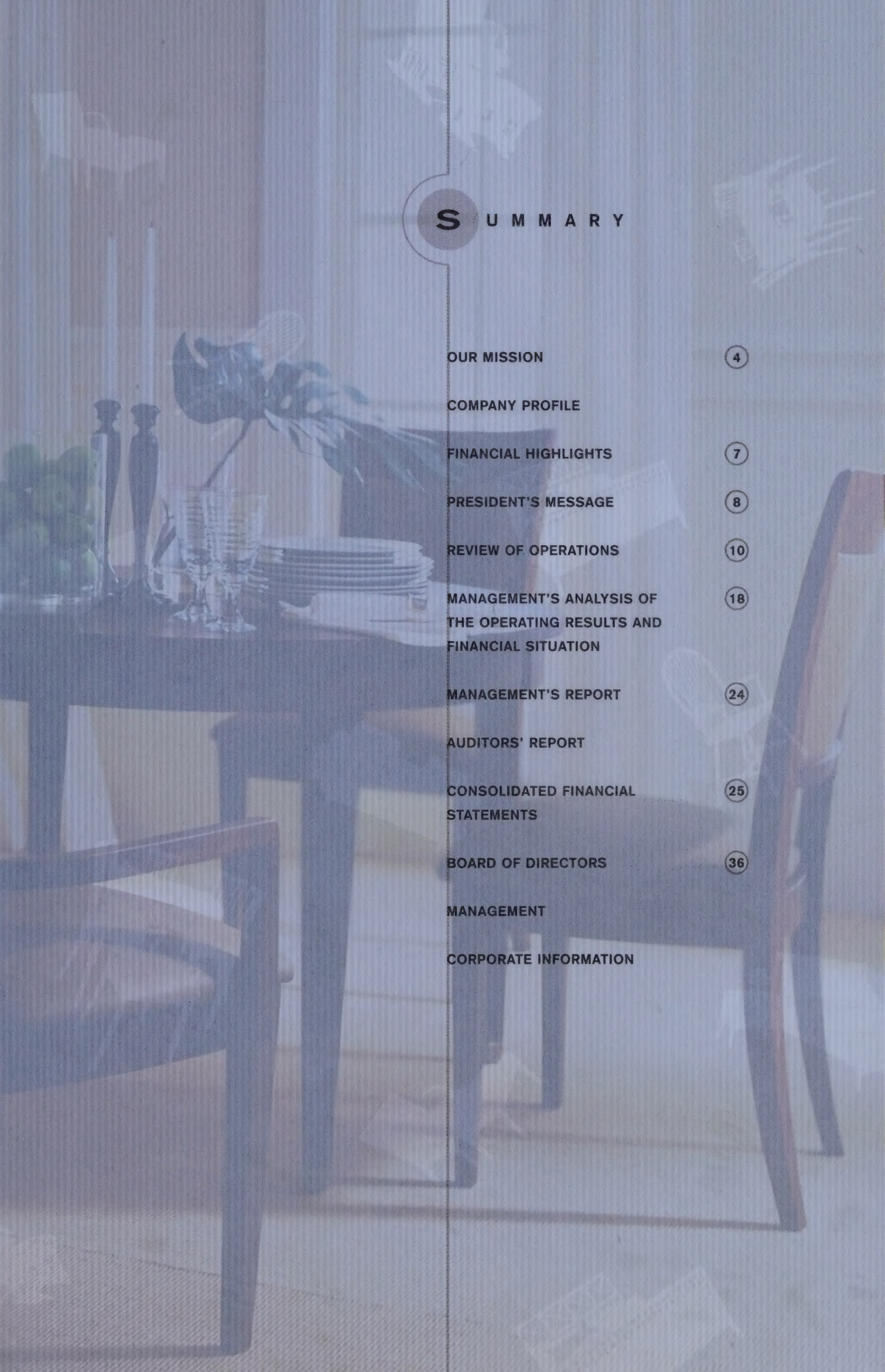
Shermag inc.

1999 - 2000

ANNUAL REPORT



SUMMARY

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1999-2000

OUR MISSION

Shermag's corporate mission is to produce the highest quality furniture available in the marketplace. While fully aware of the importance of assuring the Company's shareholders a positive return on their investment, Shermag's management is also concerned about offering fair working conditions to its 1,800 employees.

COMPANY PROFILE

Shermag is a leader in the production and distribution of high-quality residential furniture. The Company enjoys an enviable reputation in the North American market and figures prominently in the design of contemporary-style furniture.

Shermag's facilities include a network of medium-size factories equipped with state-of-the-art technology. Vertical integration — from the forest to the retailer — gives the Company an exceptional competitive edge in a highly fragmented industrial sector. Three hardwood sawmills, a plant specializing in the fabrication of components, and a veneer plant all contribute to the efficiency of the Company's ten furniture manufacturing facilities and to a lowering of production costs.

Shermag focuses on specific markets in the sale of its products. Major department stores in the United States and Canada, multiple-location chain stores specializing in the distribution of high-end furniture, as well as the best independent retailers comprise the Company's marketing targets.

March 31 2000	April 2 1999	April 3 1998	April 4 1997	March 29 1996
154,328	128,134	109,438	88,584	65,518
144,391	120,594	103,887	84,244	62,283
123,444	100,245	81,887	62,973	43,333
80%	78%	75%	71%	66%
46,319	38,383	34,025	28,590	22,542
16,665	13,105	13,098	9,597	6,160
25,373	19,519	18,256	14,183	10,538
11,106	8,704	9,507	6,468	5,193
13,208,774	13,284,674	13,282,674	11,232,674	10,382,674
0.84	0.66	0.78	0.60	0.51
0.83	0.66	0.78	0.57	0.47
5.79	4.96	4.31	1.99	1.42
7.00	9.30	18.25	12.70	4.75
8.4 x	14.1 x	23.4 x	22.2 x	10.1 x
142,735	131,556	107,382	75,686	60,403
37,299	31,057	32,969	15,094	7,337
12,205	13,224	12,760	18,114	14,087
76,976	66,378	57,662	22,799	15,156
17,912	14,186	12,252	9,795	7,976
30.01 %	29.96 %	31.09 %	32.27 %	34.41 %
7.20 %	6.79 %	8.69 %	7.30 %	7.93 %
16.44%	15.23%	16.68%	16.01%	16.08%
1.84 : 1	1.71 : 1	2.02 : 1	1.49 : 1	1.26 : 1
0.16 : 1	0.20 : 1	0.22 : 1	0.79 : 1	0.93 : 1
16%	14%	24%	34%	42%

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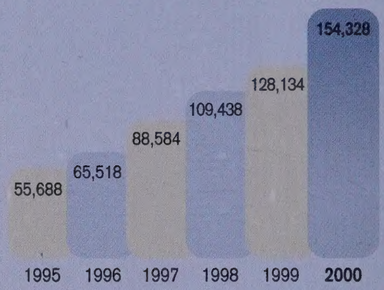
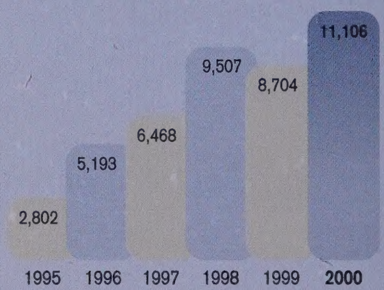
GROSS REVENUE



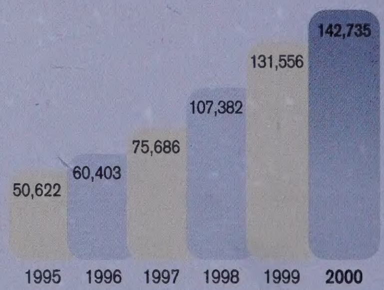
COMPOUND GROWTH RATE OVER FIVE YEARS: 22.6%

NET EARNINGS



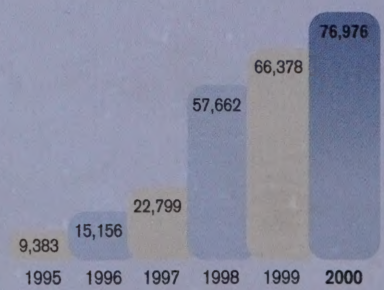
COMPOUND GROWTH RATE OVER FIVE YEARS: 31.7%

TOTAL ASSETS



COMPOUND GROWTH RATE OVER FIVE YEARS: 23.0%

SHAREHOLDERS' EQUITY

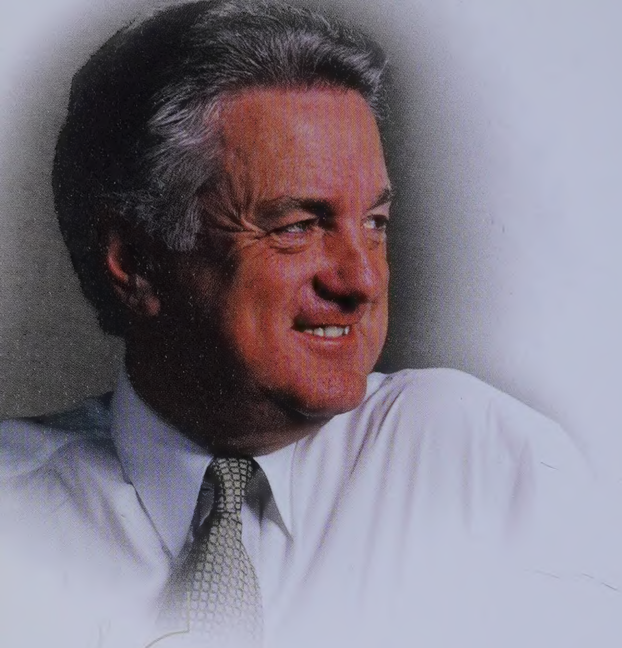


COMPOUND GROWTH RATE OVER FIVE YEARS: 52.3%

FINANCIAL HIGHLIGHTS

Year ended (in thousands of dollars, except ratios and per share data)	March 31 2000	April 2 1999	April 3 1998	April 4 1997	March 29 1996
Operating results					
Gross revenue	154,328	128,134	109,438	88,584	65,518
Net revenue	144,391	120,594	103,887	84,244	62,283
Exports	123,444	100,245	81,887	62,973	43,333
Exports as % of gross revenue	80%	78%	75%	71%	66%
Gross profit excluding depreciation and amortization	46,319	38,383	34,025	28,590	22,542
Earnings before income taxes	16,665	13,105	13,098	9,597	6,160
Earnings before interest, taxes, depreciation and amortization (EBITDA)	25,373	19,519	18,256	14,183	10,538
Net earnings	11,106	8,704	9,507	6,468	5,193
Common shares outstanding at year end	13,208,774	13,284,674	13,282,674	11,232,674	10,382,674
Earnings per share results					
Net earnings	0.84	0.66	0.78	0.60	0.51
Diluted net earnings	0.83	0.66	0.78	0.57	0.47
Book value	5.79	4.96	4.31	1.99	1.42
Market price	7.00	9.30	18.25	12.70	4.75
Price earnings ratio	8.4 x	14.1 x	23.4 x	22.2 x	10.1 x
Financial situation					
Total assets [2]	142,735	131,556	107,382	75,686	60,403
Working capital	37,299	31,057	32,969	15,094	7,337
Long-term debt [1]	12,205	13,224	12,760	18,114	14,087
Shareholder's equity	76,976	66,378	57,662	22,799	15,156
Cash flow from operations	17,912	14,186	12,252	9,795	7,976
Ratios and returns					
Gross margin	30.01 %	29.96 %	31.09 %	32.27 %	34.41 %
Net profit margin	7.20 %	6.79 %	8.69 %	7.30 %	7.93 %
EBITDA margin	16.44%	15.23%	16.68%	16.01%	16.08%
Current ratio [2]	1.84 : 1	1.71 : 1	2.02 : 1	1.49 : 1	1.26 : 1
Long-term debt ratio	0.16 : 1	0.20 : 1	0.22 : 1	0.79 : 1	0.93 : 1
Average return on equity	16%	14%	24%	34%	42%

[1] Excluding portion due within one year but including redeemable preferred shares
[2] After reclassification of accruals for advertising and volume rebate in deduction of accounts receivable



PRESIDENT'S MESSAGE

1999-2000 FISCAL YEAR

1999-2000 was another year of strong top and bottom line growth. Gross revenues were $154.3 million, up 20.4% from the previous period, pretax earnings jumped 27.2% to $16.7 million, up from $13.1 million and earnings per share were $0.84, up 27% from the previous fiscal year.

The results show solid performance, by a growth company in good financial health, which has almost doubled its size every three years for the last decade.

We are particularly pleased, given that these increases were accomplished in conjunction with cost controls in both manufacturing and selling. But as proud as we are, these achievements are but the tip of the iceberg, when compared to our Company's strong potential.

A TRANSITION YEAR: STABILITY AND SIMPLICITY

In many respects, these results cap a transition year for Shermag, during which a number of structural decisions were taken that will strengthen development prospects over the medium-to-long-term.

Shermag became in a sense, a victim of its own success. Our rapid growth rate resulted in increasingly complex management and production structures being put in place that solved immediate problems, but which eventually became cumbersome.

We thus decided to simplify operating procedures and to relearn how to do more with less. Last year, we substantially reduced the number of furniture collections offered, as well as the number of colors available, with neither decision impacting our products' market acceptance.

We also simplified decision-making processes, by delegating extensive responsibilities to the individual divisions, while concentrating strategic areas, such as financial controls, processing of information and support services at the head office level.

Now it is time to stabilize operations, in order to consolidate gains made and to ensure future growth. Changes during the previous years have caused some turmoil and movement. Each division now has in place competent, motivated and stable personnel who are confident about the future.

This quest for stability also extended to our other operations. The Year 2000 transition presented a rare opportunity to completely re-engineer and boost computer systems' capacity to support future growth. Logistical support was also greatly improved thanks to a new distribution center that was set up in Sherbrooke.

PRODUCTION

The substantial investment made in modernization and fixed assets during the past several years quickly bore fruit. So much so that, during this past year, each of our divisions was able to make a meaningful contribution to Shermag's overall success. For example, the Scotstown Division, comprising three plants, registered strong revenue growth. The Bédard Division also saw a considerable turnaround in production and sales. The Nadeau Division matured to a level that makes it a model of managerial expertise, cost control and product quality.

As for peripheral units, our sawmills as a whole were profitable last year. These contributed substantially to Shermag's success, by providing individual units with quality wood at exceptional prices.

We have also resolved difficulties in integrating new wood cutting equipment into the components plant. The new technology, developed in Germany, increases recovery on wood cutting operations by 25%, compared to other methods.

And finally, next year we will be tripling the size and capacity of the veneer manufacturing plant. This investment of nearly $5 million will provide Shermag with a source of veneer at 20% below market prices.

MARKETING

Our primary focus continues to be directed at the American market, where about 80% of our production is shipped. The segmentation strategy we have been following in regards to large American retailers has been extremely successful, and last year we were awarded the "1999 Vendor Excellence Award" from Dayton Hudson Corporation.

Canadian sales jumped 11% last year, but we are nevertheless redoubling our efforts to build our share of what, for the last few years, has been a stagnant market.

The recent nomination of a Vice-President in charge of international marketing efforts should also help boost product promotion on the international scene.

ADMINISTRATION

As mentioned above, Shermag's administration activities were considerably decentralized during the past fiscal year. Division heads now have increased responsibilities in terms of developing, manufacturing and marketing their products. The installation of a new computer system will help us better monitor the situation so weaknesses are quickly detected.

In response to the challenges posed by sustained and rapid growth, we have also reinforced upper management by creating a new level of authority. Senior Vice-Presidents were named in four sectors: production, marketing, administration and special projects. Two more positions remain to be filled.

Most importantly, we have decided to name Jeff Casselman to the newly-created position of President and Chief Operating Officer. This nomination strengthens management in light of the Company's sustained growth. Mr. Casselman will occupy the position starting August 15, 2000.

Mr. Casselman brings to our management team considerable experience in durable goods and manufacturing, as well as excellent knowledge of the North American retail market.

OUTLOOK

After having made important changes and assumed some risks, we are now entering a period of far greater stability, characterized by promising development opportunities.

There is a confluence of positive conditions in the marketplace for good short-term growth. The efficiency of our plants, our dynamic marketing strategy, product quality and sound financial health should allow Shermag to maintain sustained revenue increases for the next few years.

Long-term factors such as baby boomers and their children, who should continue to support consumption level of consumer goods for the next 15 years, are also positive. Shareholders and employees have good reason to be optimistic.

THANKS TO OUR TEAM

Shermag's continuing success is not just the result of chance. Year after year, it has been founded on the competence and loyalty of our managers and personnel, the vigilance of our Board of Directors and the renewed confidence of shareholders and clients.

At a moment where our future is more promising than ever, I want to note the contribution of each employee, board member and shareholder toward Shermag's success. This observation also extends to all of our clients who have always been faithful to the Company.

To each, I would like to express my heartfelt gratitude.

Serge Racine

Chairman of the Board
President and Chief Executive Officer

In the course of the past ten years, Shermag has based its development strategy on four fundamental elements: administrative efficiency, vertical integration of its production line, well-targeted marketing and continuously increasing productivity at each of its divisions.

Again this year, a similar approach has enabled the company to maintain a growth rate of more than 20% in gross revenues, climaxing a five-year period during which Shermag came close to tripling production. These are remarkable results for a company operating in a traditional sector where competition remains very lively across the continent.

INCREASED EFFICIENCY THANKS TO THE QUADRUPLE "S" APPROACH

Major investments by Shermag over the last few years — in acquisitions, equipment purchases, integration of new technologies and installation of new factories — exerted heavy pressures both on management processes and on production methods. It was essential that the 1999-2000 fiscal year be a period of rationalization and consolidation.

In view of this, the Company refocused its activities around a four-part policy called quadruple «S»: stability, simplicity, synchronization and profitability, represented by the dollar sign ($).

The goal of **stability** consists of enabling both staff and management at Shermag to respond harmoniously to recent changes and to enter a period of continuity that is conducive to instilling confidence while keeping growth objectives firmly in focus.

In the context of a vertically integrated business where each division is entrusted with performance of a precise task, efficiency and productivity require the constant pursuit of **simplicity** in terms of management methods and production alike.

In an industry with a growing technological component, **synchronization** is necessary to give each element in the the production chain quick access to the information required to achieve the best possible synergies.

By controlling its sources of supply in this way, Shermag is also able to provide for the particular needs of its factories in terms of the dimensions and types of wooden parts. Similarly, setting up its own veneer plant has enabled the Company to respond quickly to specific customer demands.

WELL-TARGETED MARKETING

Shermag now achieves more than 80% of its sales in the United States. This is because it has paid careful attention over the years to the quality and originality of its products, while building an effective marketing strategy and establishing true business partnerships with its U.S. customers.

Shermag's marketing strategy in the United States is based on a segmentation of the market into four specific categories: A (major department store chains); B (large independent furniture dealers); C (national North American mass market chains); and D (independent stores). Not only does this type of segmentation offer the best possible market protection through the exclusivity of Shermag products and control over the distribution of its collections in a given territory, but it also favours higher profit margins for its business partners.

REVIEW OF OPERAT

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It becomes obvious that these three S's are all oriented to a fourth element, the **$** symbolizing improvement in Shermag's profitability.

To support these goals, the Company took a number of initiatives during the last fiscal year.

It began with a restructuring of the management team. A new sharing of responsibilities was established between the Senior Vice-Presidents responsible for administration, marketing, production and special projects. A management committee was created for close monitoring of the activities of each division and the company as a whole.

The opening of a new distribution centre in Sherbrooke, replacing the Victoriaville centre, will provide for more efficient management of furniture warehousing and delivery. With its floor area of 120,000 square feet and a storage capacity of more than 500,000 cubic feet, this centre will handle the distribution of furniture manufactured at Shermag's ten plants. Thanks to this new facility, deliveries can now be carried out more frequently and more economically for customers.

To anticipate the growing needs of its customers and to provide them with better service, the Company has also set up a production planning system. It has taken measures to consolidate its design collections and to rationalize its product lines to improve production efficiency and inventory management. In this same context, the Company has created a training and support program to increase value-added in its relations with customers.

VERTICAL INTEGRATION

Shermag's sustained growth and profitability depend largely on the tight control which the Company exerts over its sources of supply. More than 90% of the hardwood it uses is produced at its own sawmills, ensuring greater price stability for its raw material and protecting it from sudden, massive price hikes similar to what the market experienced during the last fiscal year.

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Today's success is due to Shermag's marketing strategy initially implemented in category A stores. An expanding collection has led to both increasing exposure as well as escalating penetration within this category. In addition, Shermag's strategy has resulted in an augmented client base.

Category B stores continue to offer room for expansion. In order to increase its presence in this market, Shermag has implemented new collections tailored to this segment.

Recently, Shermag's largest growth occurred in category C retail stores. Penetration within this category should remain strong in the foreseeable future.

Finally, implemented transportation logistic allows Shermag to better serve their category D customers. As they do for category B stores, Shermag tailors collections to category D clients in order to boost its market share.

EFFICIENT AND PRODUCTIVE DIVISIONS

Scotstown Division

The Scotstown Division increased its revenues by 30%, a growth rate due largely to the Scotstown plant returning to the division of the same name after being temporarily attached to the Nadeau Division. Without this plant's contribution, the growth of the Scotstown Division would have been 16%.

During the last fiscal year, the Scotstown Division has successfully completed the rationalization of its production lines. This way it could achieve greater stability in its production processes, better quality in its products and improved customer service.

The Scotstown Division is currently working on the development of new collections made of different wood species. This will eventually enable it to reduce the cost of raw materials.

Nadeau Division

The Nadeau Division, which includes the Saint-François-de-Madawaska and Edmundston plants in New Brunswick, recorded 8% revenue growth in the last fiscal year.

Production at the Saint-François-de-Madawaska plant increased by 15%. The new Edmundston plant had the fastest start-up in Shermag's history and has already achieved a good degree of stability, with revenues comparable to the Scotstown plant, from which it took over.

The Nadeau Division enjoys excellent management and production teams, stable collections and customers, as well as a strongly rooted culture of quality.

The Division is currently preparing new collections based on different wood species to diversify its sources of supply and to reduce demand for certain varieties.

HPL Division

Production at the HPL plant remained stable compared to the previous fiscal year. The launch of the *Orléans* collection and the start of dining room table production created a temporary decline in productivity and production. This affected sales volume. However, a significant increase in HPL's production and sales is expected in the coming months. An evening shift will be added soon in anticipation of the opening of a new plant in a building already belonging to Shermag in Victoriaville. The Victoriaville plant remains among Shermag's most stable ones.

Chandéric / Conant Ball Division

The Chandéric / Conant Ball Division manufactures glider rockers in its Lennoxville plant. Revenues in the last fiscal year remained stable compared to the previous fiscal year.

Chandéric has benefited from major investments in equipment during the last few years, enabling it to improve its efficiency quite considerably. Although it has a solid management team with a mastery of production processes, this Division currently depends too heavily on just a few big accounts. In the future, it will have to put renewed effort into finding new customers who are likely to provide greater stability.

Bédard Division

After a somewhat difficult integration process, the Bédard Division achieved a spectacular recovery in its situation during the last fiscal year, with 26% revenue growth.

This recovery is due largely to the initiatives taken by a specialized working group set up last year. The Division's three plants now benefit from better control over production processes and simplified management structures and systems, as well as better synchronization that has helped achieve a strong improvement in productivity.

Thanks to new raw materials, new customers and new high-end products, the Bédard Division's profitability outlook is clearly improved.

Sofas International

Sofas International had a truly exceptional year with a doubling of its revenues. Besides improving its productivity with a tightening of production costs, it also broadened and diversified its product range.

New facilities and an innovative product will help this Division increase its sales volume considerably over the coming years, especially in the U.S. market which it has not really exploited up to now. The Company has high hopes for the *Caméléon*. This product is remarkable because of its simplicity and its innovative character and should contribute exceptionally well to Shermag's future profits.

Mégabois / Montauban / Woodtek

In the last fiscal year, Shermag continued to benefit from a mostly independent wood supply, giving the Company a marked advantage over its competitors by helping it absorb market fluctuations. In 1999-2000, Shermag obtained 90% of its hardwood from its own sawmills. It is planning to raise this proportion even higher starting in the next fiscal year. To achieve this, the Company is planning to reduce the production of wood by-products at Woodtek in order to provide greater availability of hardwood for the Group's factories.

This independent supply, however, must not be attained at the cost of the sawmills' earnings. This is why Shermag intends to maintain an equitable level for transfer prices of wood from the sawmills to the factories.

Placages Lennox

The Placages Lennox plant supplies Shermag's divisions with a broad range of components. It represents a significant element in the Company's vertical integration.

Despite the fact that it is operating at full capacity, this Division is managing to meet only 80% of the Group's requirements. This is why the plant will be expanded during the 2000-2001 fiscal year. The expansion will add 25,000 square feet to the plant's current floor space, allowing for a tripling of its area and its production capacity.

This represents an investment of close to $5 million that will enable Shermag to supply itself with veneer at costs 20% lower than current market prices.

PUBLIC SHARE BUYBACK OFFER

Last August, Shermag announced its decision to proceed with a public offer to buy back common shares in the normal course of activities. After obtaining approval from the pertinent authorities, the Company set the buyback period from September 2, 1999 to September 1, 2000, for a maximum buyback of 664,283 common shares, representing 5% of outstanding shares. At the end of the fiscal year, 76,900 shares had been bought back, at an average price of $6.69.

Operating results

Gross revenue for the year ended March 31, 2000 reached $154.3 million, up 20.4% from $128.1 million the previous year. Compound annual growth rate of the past five years stands at 22.6%.

About 80% of sales are to the United States, the balance to Canada. Sales to the United States jumped 23.1% and Canadian sales were up 10.7% compared with last fiscal year.

PROFITABILITY

Net earnings for the year increased to $11.1 million or 7.2% of gross sales, compared to $8.7 million, or 6.8% of revenues in 1998-1999. Net earnings increased by 27.6% from the previous year. Fully diluted net earnings per share increased from $0.66 a share in 1998-1999 to $0.83 per share in 1999-2000.

Gross margin as a percentage of revenue remained at 30%, a more than satisfactory performance considering the Company's high revenue growth rate of 23% during recent years, coupled with the integration and running-in of new plants and the addition of new products into the mix.

Operating costs as a percentage of gross revenues dropped from 19.7% to 19.2%. Selling and administrative expenses increased by only 8.1% during the year and now total 12.9% of revenues, compared to 14.4% in 1998-1999.

Financial expenses rose a little more than $1 million, half of this total resulting from a larger foreign exchange loss and the other half due to a more important use of the line of credit. Depreciation rose $1.8 million from last year due to substantial investments in fixed assets during the past two years.

Investments

Since May 29, 1997, the Company has held a 50% interest in the Scierie Montauban Inc., which specializes in hardwood. On October 2, 1999, Shermag increased its participation to 100% by buying out its partner for $600,000 in cash. The cash used in this transaction, after deducting the cash and cash equivalents items in the acquired company was $369,000.

Investments totaling $7.3 million were made in fixed assets including $2.9 million deployed in the acquisition and fitting out of a new warehouse and distribution center in Sherbrooke. Other investments totaling $3.6 million were allocated to increase capacity or improve manufacturing processes in certain plants. Finally, $724,000 was invested to maintain and develop the computer systems in place, including Y2K compliance.

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CHANGES IN FINANCIAL POSITION

During the year cash and cash equivalents amounts rose $2.5 million. Cash generated comes from three sources:

Operations

Cash flow from operations totaled $17.9 million in 1999-2000. Of this, $4.8 million was used to support working capital items. Net cash generated from operations was thus $13.1 million.

Financing

Financing activities used up $1.2 million of cash. In addition, $2.7 million was applied toward repaying term loans, according to their repayment terms and short-term borrowing increased $1.9 million.

The Company also purchased 76,900 of its own outstanding common shares at an average price of $6.69 each, for a total disbursement of $515,000, as part of a public buyback offering to common shareholders. The excess paid over the book value of these shares, valued at $298,000, is shown in the retained earnings section as a premium on stock buybacks. The Company may, as part of this public buyback offer, purchase a maximum of 664,283 common shares over a 12-month period ending September 1, 2000.

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FINANCIAL POSITION

In comparing the Company's March 31, 2000, financial position with that existing on April 2, 1999, certain facts should be noted:

- The Company's net and gross profit margins have improved slightly.
- Working capital increased $6.2 million and the current ratio increased from 1.71:1 to 1.84:1.
- The Company's total debt increased only $581,000.
- Cash flow from operations totaled $17.9 million.
- Total assets increased $11.2 to $142.7 million.
- Shareholder's equity increased $10.6 million, jumping from $66.4 million to $77 million.

The Company's financial position continues to improve. On March 31, 2000 the Company has an unused line of credit. Its borrowing power has improved since the level of guarantee attached to the loans has increased and is more than enough relative to the level of credits authorized and used. All the financial ratios required by the credit agreement in place with the bank have been respected.

YEAR 2000

Conversion of the Company's systems to the Year 2000 compliance was achieved without any significant incident, and like many others, we are happy to finally be working on other things.

RISKS AND UNCERTAINTIES

Shermag has had in place for several years a policy designed to protect the Company against significant currency fluctuations. Any excess funds carried in U.S. dollars are thus hedged using financial instruments such as forward exchange contracts. The Company feels adequately protected and fluctuations in the U.S. currency are not a preoccupation for the next twelve months.

The Company will be more exposed to fluctuations in raw material prices or supplies and will have to take measures to increase its self-sufficiency by increasing its vertical integration or concluding strategic alliances with solid business partners.

The Company's potential and its administrative cohesion, which are both improving daily, are indications of several years of sustained growth.

Josée Girard

Josée Girard, CA
Comptroller

MANAGEMENT'S REPORT

Shermag Inc.'s consolidated financial statements for the years ended March 31, 2000 and April 2, 1999 and the financial information included in this annual report are the responsibility of management. The consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada and with the policies set forth in the notes to said statements.

The Audit Committee of the Board is responsible for reviewing the consolidated financial statements in detail, for ensuring that the Company's internal control systems, management policies and accounting practices are adhered to, and for recommending approval of the consolidated financial statements to the Board of Directors.

The chartered accountants, Raymond Chabot Grant Thornton, have audited the consolidated financial statements which appear hereinafter and their report indicates the extent of their audit and their opinion on said consolidated financial statements.

Serge Racine
Chairman of the Board, President
and Chief Executive Officer

Josée Girard

Josée Girard, CA
Comptroller

AUDITORS' REPORT

To the Shareholders of Shermag Inc.

We have audited the consolidated balance sheets of Shermag Inc. as at March 31, 2000 and April 2, 1999 and the consolidated statements of earnings, retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at March 31, 2000 and April 2, 1999 and the results of its operations and its cash flows for the years then ended in accordance with generally accepted accounting principles.

Raymond Chabot Grant Thornton

General Partnership
Chartered Accountants

Sherbrooke, Québec
May 19, 2000

1999-2000

Shermag inc.

CONSOLIDATED FINANCIAL STATEMENTS

CONSOLIDATED EARNINGS

Years ended March 31, 2000 and April 2, 1999

(Amounts in thousands of dollars, except earnings per common share)

	2000-03-31	1999-04-02
	$	$
Gross revenue	**154,328**	128,134
Less: returns, allowances and discounts	**9,937**	7,540
Net revenue	**144,391**	120,594
Cost of sales	**98,072**	82,211
Gross profit excluding depreciation and amortization	**46,319**	38,383
Selling and administrative expenses	**19,896**	18,398
Financial expenses	**3,761**	2,640
Depreciation and amortization	**5,997**	4,240
	29,654	25,278
Earnings before income taxes	**16,665**	13,105
Income taxes (Note 5)	**5,559**	4,401
Net earnings	**11,106**	8,704
Net earnings per common share	**0.84**	0.66
Diluted net earnings per common share	**0.83**	0.66
Average weighted number of common shares	**13,276,097**	13,282,718

CONSOLIDATED RETAINED EARNINGS

Years ended March 31, 2000 and April 2, 1999

(Amounts in thousands of dollars)

	2000-03-31	1999-04-02
	$	$
Balance, beginning of year	**28,532**	19,828
Net earnings	**11,106**	8,704
	39,638	28,532
Premium on redemption of common shares	**298**	
Balance, end of year	**39,340**	28,532

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED CASH FLOWS

Years ended March 31, 2000 and April 2, 1999
(Amounts in thousands of dollars)

	2000-03-31	1999-04-02
	$	$
OPERATING ACTIVITIES		
Net earnings	**11,106**	8,704
Non-cash items		
Gain on disposal of assets		(10)
Amortization of deferred credits	**(268)**	(114)
Other depreciation and amortization	**5,997**	4,240
Deferred income taxes	**1,077**	1,366
Changes in working capital items (Note 4)	**(4,832)**	(9,894)
Cash flows from operating activities	**13,080**	4,292
INVESTING ACTIVITIES		
Business acquisitions (Note 6)	**(369)**	(4,254)
Fixed assets	**(7,316)**	(15,329)
Disposal of fixed assets	**60**	39
Deferred charges	**(1,782)**	(1,767)
Deferred credits	**16**	501
Cash flows from investing activities	**(9,391)**	(20,810)
FINANCING ACTIVITIES		
Net change in bank loans and acceptances	**1,940**	13,531
Long-term loans	**49**	13,284
Instalments on long-term debt	**(2,684)**	(13,549)
Issue of shares	**7**	12
Redemption of shares	**(515)**	
Cash flows from financing activities	**(1,203)**	13,278
Net increase (decrease) in cash and cash equivalents	**2,486**	(3,240)
Cash and cash equivalents, beginning of year	**(1,697)**	1,543
Cash and cash equivalents, end of year	**789**	(1,697)

The accompanying notes are an integral part of the consolidated financial statements.

CONSOLIDATED BALANCE SHEETS

March 31, 2000 and April 2, 1999

(Amounts in thousands of dollars)

	2000-03-31	1999-04-02
	$	$
ASSETS		
Current assets		
Cash	**789**	
Accounts receivable (Note 7)	**31,065**	28,784
Inventories (Note 8)	**49,104**	45,320
Prepaid expenses	**842**	582
	81,800	74,686
Fixed assets (Note 9)	**57,741**	53,858
Other assets (Note 10)	**3,194**	3,012
	142,735	131,556
LIABILITIES		
Current liabilities		
Outstanding cheques		1,697
Bank loans and acceptances (Note 11)	**27,010**	25,070
Accounts payable and accrued liabilities	**14,972**	15,138
Income taxes payable	**1,712**	45
Instalments on long-term debt	**807**	1,679
	44,501	43,629
Long-term debt (Note 12)	**12,205**	13,224
Deferred income taxes	**5,112**	4,132
Deferred credits (Note 13)	**3,941**	4,193
	65,759	65,178
SHAREHOLDERS' EQUITY		
Capital stock (Note 14)	**37,636**	37,846
Retained earnings	**39,340**	28,532
	76,976	66,378
	142,735	131,556

The accompanying notes are an integral part of the consolidated financial statements.

On behalf of the Board,

Serge Racine
Director

Arthur P. Earle
Director

1 - GOVERNING STATUTES AND NATURE OF OPERATIONS

The Company, incorporated under Part IA of the Companies Act (Québec), manufactures furniture.

2 - ACCOUNTING POLICIES

Principle of consolidation

The financial statements include the accounts of the Company and its wholly-owned subsidiaries.

Cash and cash equivalents

The Company's policy is to present cash and temporary investments having a term of less than three months from the acquisition date with cash and cash equivalents.

Inventory valuation

Finished goods and goods in process are valued at the lower of cost and net realizable value. Cost is determined by the average cost method.

Raw materials and supplies are valued at the lower of cost and replacement cost. Cost is determined by the first in, first out method.

Depreciation and amortization

Fixed assets are depreciated over their estimated useful lives according to the following methods, periods and annual rates:

	Methods	Periods and rates
Buildings	Straight-line	40 years
Machinery and equipment	Diminishing balance	10%
Rolling stock and software	Diminishing balance	30%
Office furniture	Diminishing balance	20%
Leasehold improvements	Straight-line	5 years
Forestry properties	Straight-line	25 years

Deferred charges are amortized according to the straight-line method over periods not exceeding five years.

Goodwill represents the excess of cost over the fair value of net assets acquired, and is amortized according to the straight-line method over a period of ten years until 2003. The valuation and amortization of goodwill are revised regularly by management to ensure that no decrease in the value has occurred, by comparing the accounting value with the non-actualized future cash flows generated by those assets.

Deferred credits represent government grants and investment tax credits resulting from the acquisition of fixed assets. The grants and tax credits are accounted for as deferred credits and amortized according to the same annual methods and rates as the assets to which they relate are depreciated.

Income taxes

The Company follows the deferred income tax allocation method in providing for income taxes. Under this method, timing differences between income for accounting purposes and income for tax purposes give rise to deferred income taxes.

The Company does not provide for income taxes on undistributed earnings of the foreign subsidiary as these earnings are being reinvested in such local operations.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of the contingent assets and liabilities and the reported amounts of revenues and expenses. Actual results could differ from these estimates.

Earnings per common share

The calculation of basic net earnings per common share is based on the weighted average number of outstanding shares during the years. The fully diluted net earnings per common share take into account all elements having a possible dilution effect.

(Amounts in the tables are in thousands of dollars)

Foreign currency translation

Monetary assets and liabilities in foreign currency are translated at exchange rates in effect at the balance sheet dates, whereas other assets and liabilities are translated at exchange rates in effect at transaction dates. Revenue and expenses in foreign currency are translated at the monthly average rate in effect, with the exception of depreciation, which is translated at the historical rate. Gains and losses are included in the earnings for the years.

Assets and liabilities of the self-sustaining foreign subsidiary are translated into Canadian dollars at the exchange rate in effect at the balance sheet dates. Revenue and expenses are translated at the average rate in effect during the years. Gains and losses are included in the "Accumulated exchange adjustments" account of the shareholders' equity, if applicable.

Forward exchange contracts

The Company enters into foreign exchange contracts to manage its currency risk exposure. These financial instruments are presented at cost. Positions hedged by foreign exchange contracts are converted using the contract rate and the gains or losses are recognized to earnings during the years in which the revenues or expenses resulting from the corresponding hedged position are recorded.

3 - INFORMATION INCLUDED IN THE STATEMENT OF EARNINGS

	2000-03-31	1999-04-02
	$	$
Depreciation of fixed assets	**4,397**	3,055
Amortization of deferred charges	**1,546**	1,131
Amortization of goodwill	**54**	54
Amortization of deferred credits	**268**	114
Interest on short-term debt	**1,805**	1,385
Interest on long-term debt	**906**	789
Loss on foreign exchange	**1,050**	466

4 - INFORMATION INCLUDED IN THE STATEMENT OF CASH FLOWS

The changes in working capital items are detailed as follows:

	2000-03-31	1999-04-02
	$	$
Accounts receivable	**(2,175)**	(5,202)
Inventories	**(3,741)**	(3,414)
Prepaid expenses	**(205)**	(20)
Accounts payable and accrued liabilities	**(378)**	(240)
Income taxes payable	**1,667**	(1,018)
	(4,832)	(9,894)

Cash flows relating to interest and income taxes on operating activities are detailed as follows:

	2000-03-31	1999-04-02
	$	$
Interest paid	**2,555**	1,943
Income taxes paid	**2,815**	3,873

The Company has applied retroactively the recommendations of the Canadian Institute of Chartered Accountants with regards to the presentation of its cash flows. These new recommendations require a redefinition of cash and cash equivalents. The application of these new recommendations results in the net change in bank loans and acceptances being presented with financing activities. Previously, bank loans and acceptances were considered to be part of cash and cash equivalents.

(Amounts in the tables are in thousands of dollars)

5 - INCOME TAXES

The difference between the Company's effective income tax rate and the combined Federal and Provincial income tax rate in Canada is explained as follows:

	2000-03-31	1999-04-02
	%	%
Income taxes at the combined Federal and Provincial income tax rate in Canada	**39.6**	39.3
Manufacturing and processing profits deduction	**(6.8)**	(6.7)
Permanent differences and other	**0.6**	1.0
Income taxes at the Company's effective income tax rate	**33.4**	33.6

	2000-03-31	1999-04-02
	$	$
Income taxes are detailed as follows:		
Current	**4,482**	3,035
Deferred	**1,077**	1,366
	5,559	4,401

The tax benefit resulting from allowable capital losses is not recorded in the financial statements. These losses amount to $2,647,000 and may be carried-forward and applied against taxable capital gains over an indefinite period.

6 - BUSINESS ACQUISITIONS

On October 2, 1999, the Company increased to 100% its share in a joint venture, Scierie Montauban Inc. which operates a hardwood sawmill, for an amount of $600,000 in cash.

On February 23, 1999, the Company acquired certain operating assets from a company operating a sawmill in North Anson, Maine, for an amount of $4,253,599 ($2,893,600 US) in cash.

These acquisitions were accounted for according to the purchase method. The results of operations since the dates of acquisition have been included in these consolidated financial statements. The above-mentioned net operating assets acquired are detailed as follows:

	2000-03-31	1999-04-02
	$	$
Current assets	**435**	2,236
Fixed assets	**1,024**	2,018
Deferred income taxes	**97**	
Current liabilities	**(212)**	
Long-term debt	**(744)**	
Acquisition cost	**600**	4,254
Cash and cash equivalents acquired	**(231)**	
Decrease in cash and cash equivalents following these acquisitions	**369**	4,254

7 - ACCOUNTS RECEIVABLE

	2000-03-31	1999-04-02
	$	$
Trade accounts		
Canada	**5,997**	5,185
United States	**23,339**	21,307
	29,336	26,492
Sales taxes receivable	**1,108**	1,731
Others	**621**	561
	31,065	28,784

88% of the United States trade accounts receivable are secured by a global multirisk insurance policy upon shipping.

(Amounts in the tables are in thousands of dollars)

8 - INVENTORIES

	2000-03-31	1999-04-02
	$	$
Finished goods	**22,075**	20,987
Goods in process	**12,681**	11,409
Raw materials	**12,799**	11,653
Supplies	**1,549**	1,271
	49,104	45,320

9 - FIXED ASSETS

			2000-03-31
	Cost	**Accumulated depreciation**	**Net**
	$	**$**	**$**
Land	**2,150**		**2,150**
Buildings	**27,168**	**4,155**	**23,013**
Machinery and equipment	**39,213**	**12,872**	**26,341**
Rolling stock	**1,214**	**704**	**510**
Office furniture	**5,263**	**3,041**	**2,222**
Software	**4,224**	**1,357**	**2,867**
Leasehold improvements	**454**	**411**	**43**
Forestry properties	**696**	**101**	**595**
	80,382	**22,641**	**57,741**

			1999-04-02
	Cost	Accumulated depreciation	Net
	$	$	$
Land	1,847		1,847
Buildings	23,555	3,549	20,006
Machinery and equipment	35,908	10,161	25,747
Rolling stock	1,009	505	504
Office furniture	4,682	2,620	2,062
Software	3,749	805	2,944
Leasehold improvements	454	305	149
Forestry properties	631	32	599
	71,835	17,977	53,858

10 - OTHER ASSETS

	2000-03-31	1999-04-02
	$	$
Deferred charges, at amortized cost		
New product development costs	**1,132**	1,124
Start-up costs	**673**	1,017
Promotional tools	**1,112**	508
Financing charge	**116**	148
	3,033	2,797
Goodwill, at amortized cost	**161**	215
	3,194	3,012

(Amounts in the tables are in thousands of dollars)

11 - BANK LOANS AND ACCEPTANCES

The Company has total authorized operating credits of $32,500,000, which can be used as bank loans or acceptances. These amounts can be drawn out in Canadian or American dollars. The bank loans bear interest at prime rate or US prime rate, and this rate is reviewed on a quarterly basis. The bank acceptances are at the market rate. The operating credits are established for a three-year term, renewable on September 30 of each year for an additional year and are subject to the restrictions mentioned in Note 12(*).

12 - LONG-TERM DEBT

	2000-03-31	1999-04-02
	$	$
Loan, prime rate plus 0.5%, payable in quarterly capital instalments of $300,000 starting February 2001, maturing no later than 2003 (*)	**11,300**	12,200
Loans, secured by immovable assets and machinery, prime rate plus 0.5% to 2%, payable in varying monthly instalments until 2004	**220**	1,049
Loan, lender's prime rate, payable in monthly capital instalments of $13,649, maturing in 2001	**232**	396
Non-interest bearing loans, payable in annual instalments, maturing at various dates until 2007	**1,260**	1,258
	13,012	14,903
Instalments due within one year	**807**	1,679
	12,205	13,224

(*) This loan and the short-term bank loans and acceptances are secured by a first rank mortgage on the universality of all present and future movable and immovable, tangible and intangible assets, for an amount of $70,000,000. The Company is subject to certain restrictions under the credit agreement. The Company was in compliance with these restrictions as at March 31, 2000.

The instalments on long-term debt for the next five years are $807,079 in 2001, $1,478,483 in 2002, $1,421,795 in 2003, $8,826,780 in 2004 and $216,820 in 2005.

13 - GOVERNMENT ASSISTANCE

In 1999, the Company obtained from the Department of Economic Development and Tourism of New Brunswick, a $2,000,000 contribution relating to investments in fixed assets.

This government contribution was reported and presented in the balance sheet as deferred credits. This contribution could be redeemable in part if the Company does not maintain a certain number of jobs during a twelve-month period ending on December 31, 2001.

(Amounts in the tables are in thousands of dollars)

14 - CAPITAL STOCK

Authorized

Unlimited number of common shares, without par value, voting and participating

Unlimited number of preferred shares of first and second rank, without par value, which can be issued in one or more series, for which the directors will determine their number, designation, rights, privileges, conditions and restrictions

Preferred shares of second rank, series 1, annual and non-cumulative dividend of $0.06 per share, non-voting, non-participating, redeemable at the Company's option at the paid-up capital amount

	2000-03-31		1999-04-02	
	Number of shares	**Amount**	Number of shares	Amount
		$		$
Issued and fully paid				
Common shares				
Balance, beginning of year	**13,284,674**	**37,397**	13,282,674	37,385
Stock options exercised for cash	**1,000**	**7**	2,000	12
Redemption of shares for cash	**(76,900)**	**(217)**		
Balance, end of year	**13,208,774**	**37,187**	13,284,674	37,397
Preferred shares of second rank, series 1				
Balance, beginning and end of year	**700,000**	**449**	700,000	449
		37,636		37,846

The Company has reserved 500,000 common shares as a stock option plan for directors and officers. The period, terms and conditions of these options are determined by the Board of Directors provided that the options expire at the latest 10 years following the date they are granted.

The Company's stock option plan is as follows:

	2000-03-31		1999-04-02	
	Options	**Weighted average exercice price**	Options	Weighted average exercice price
		$		$
Options outstanding, beginning of year	**315,500**	**13,09**	217,500	12,15
Granted	**122,000**	**7,22**	100,000	15,00
Exercised	**(1,000)**	**6,60**	(2,000)	6,25
Cancelled	**(100,000)**	**7,10**		
Options outstanding, end of year	**336,500**	**12,76**	315,500	13,09

Summary of options outstanding at March 31, 2000:

Total outstanding				Total exercisable	
Options	Exercise price	Weighted average exercise price	Contractual remaining life	Options	Weighted average exercise price
	$	$			$
57,000	6,25 - 9,00	6,89	6,6 years	32,000	6,39
279,500	13,20 - 17,00	13,96	6,1 years	209,500	13,91

(Amounts in the tables are in thousands of dollars)

15 - COMMITMENTS

The Company has entered into long-term lease agreements, expiring at the latest in 2005, which call for lease payments of $2,400,813 for the rental of premises. Minimum lease payments for the next five years are $411,669 in 2001 and $442,032 in 2002, 2003, 2004 and 2005.

16 - FAIR VALUE OF THE FINANCIAL INSTRUMENTS

Primary financial instruments

Cash, accounts receivable, outstanding cheques, bank loans and acceptances, accounts payable and accrued liabilities are short-term financial instruments whose fair value approximates their carrying amount given that they will mature shortly.

The estimated fair value of the Company's long-term debt is determined based on analysis of the discounted value of cash flows, using interest rates in effect for the Company's similar borrowing agreements. The carrying amount is $13,011,855 ($14,902,708 as at April 2, 1999) and there is no material difference with the fair value.

Derivative financial instruments

As at March 31, 2000, the Company is committed, by virtue of forward exchange contracts, to sell $95,000,000 ($95,000,000 as at April 2, 1999) US dollars for Canadian dollars. The fair value of the derivative financial instruments is determined based on prices obtained from the Company's brokers for identical or similar financial instruments. The forward exchange contracts are detailed as follows:

			2000-03-31
Term	**$ US**	**Average rate**	**Fair value**
	$		**$**
1 to 12 months	**54,000**	**1,5164**	**3,998**
13 to 21 months	**41,000**	**1,4570**	**1,064**
	95,000	**1,4908**	**5,062**

			1999-04-02
	$ US	Average rate	Fair value
	$		$
1 to 12 months	59,000	1,4378	(2,569)
13 to 21 months	36,000	1,5397	4,308
	95,000	1,4764	1,739

17 - GEOGRAPHIC BREAKDOWN OF REVENUE

The Company's revenue can be broken down geographically as follows:

	2000-03-31	1999-04-02
	$	$
Canada	**30,884**	27,889
United States	**123,444**	100,245
	154,328	128,134

BOARD OF DIRECTORS

Serge Racine (1) (3)
Chairman of the Board, President and Chief Executive Officer Shermag Inc.

Charles Chamard (2) (3)
Corporate Director

Arthur P. Earle, C.M., FEIC (1)
Consultant

Jean-Côme Gaudet (2)
Management Consultant

Jacques A. Nadeau (2) (3)
Senior Vice-president
MédiSolution

Claude Pichette (1)
Counselor, Conflicts and Litigation Huis Clos Ltée

John D. Thompson (1)
Deputy Chairman
Montréal Trust

Jeanne Wojas (3)
Lawyer and Corporate Director

(1) Member of the Executive Committee
(2) Member of the Audit Committee
(3) Member of the Human Resources Committee

MANAGEMENT

Serge Racine
Chairman of the Board, President and Chief Executive Officer Shermag Inc.

Josée Bélanger
Corporate Secretary

Guy Cardinal
Vice-president, Production

Josée Girard
Comptroller

Denis Malaket
Vice-president, Administration

Claude Sauvé
Vice-president, Special projects

CORPORATE INFORMATION

Transfer Agent
General Trust of Canada
1100, rue University
Montréal (Québec)
H3B 9Z9

Auditors
Raymond Chabot Grant Thornton
Sherbrooke (Québec)

Bank
National Bank of Canada

Stock Registration
Shermag Inc.'s shares are listed on the Toronto Stock Exchange under symbol SMG.

Annual Information Form and General Information
To obtain a copy of the Annual Information Form submitted to the Québec Securities Commission and the Ontario Securities Commission or for any additional information regarding the Company, please send a written request to the Company's Secretary or to the Transfer Agent.

Annual and Special General Meeting of Shareholders
Thursday, August 24, 2000 at 16:00
Club Saint-Denis
257, rue Sherbrooke Est
Montréal (Québec)

DIVISIONS

BÉDARD

Émile Hudon, President

726, rue Principale
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825, boul. Industriel
Granby (Québec)
J2J 1A5

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Sainte-Gertrude (Québec)
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chanderic
CONANT BALL

Benoit Racine, President

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nadeau

Aurèle Turcotte, President

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HPL MOBILIER FURNITURE

Aurèle Turcotte, President

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G6P 6M8

Scotstown

Denis Charest, President

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Bishopton (Québec)
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510, rue Saint-François
Disraeli (Québec)
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Placages Lennox

André Beauregard, Manager

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General Manager

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Daniel Lefebvre
General Manager

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Daniel Lefebvre
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